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PW PREDICTS

Roberts S. Reichard, executive editor

Bargaining clout continues

Inflationary pressures aren't as muted as last year, but there's still no suggestion of a new upward price spiral.

The dollar seems to be stabilizing. While import prices are still rising, increases should soon begin to taper off—if not over the next few months, then by early next year.

Another fundamental determinant of inflation—labor costs—also suggests that things are under control. Average hourly earnings advanced at an annual rate of 1.9% in the first quarter of 1987 and 3.1% in the second quarter. That's slightly higher than last year—not bad considering the jobless rate has been edging lower. And the trend is likely to continue: Major collective bargaining agreements in the first half of 1987 produced only a 2.1% average first year increase, and only 2.5% annually over the life of the contract.

Even these modest increases are being substantially offset by efficiency gains. Nonfarm productivity is picking up steam again—rising for two straight quarters after staying relatively flat for a year. Even more significant is manufacturing. Recent productivity gains are impressive—3.1% at annual rate in the first quarter and 3.3% in the second quarter. Implication: Unit labor costs for many manufacturers remain relatively stable—not like the late 1970s and early 1980s when annual increases were in the double-digit range.

All the above is not meant to imply a repeat of last year when producer prices actually fell. Energy prices are rising (in contrast to last year's declines) as are other key raw materials sectors such as metals, chemicals, and paper.

Purchasing managers, however, remain optimistic. The latest N.A.P.M. Business Survey Committee report, monitoring buyers from 250 firms, sees average procurement costs rising only 2.3% over the second half of 1987. This suggests some deceleration from the first half when these same PMs said their prices rose an average of 3.4%.

If correct, purchasing executives will experience an overall procurement cost rise of about 5.5% for the 12-month period ending in December. Again, that's not bad considering we are now completing the fifth straight year of business recovery.

The results of a new *PurchasingWorld* survey on off-list pricing are also indicative of continued buyer bargaining clout. While bargains aren't quite as easy to find as last year, the typical PM still manages to shave about 6% off his list prices. More than half of those surveyed feel they'll be able to hold onto or improve upon concessions in the year ahead.

What does it all add up to? Barring a new Mid-East blowup, there won't be a big inflationary surge.

Steel

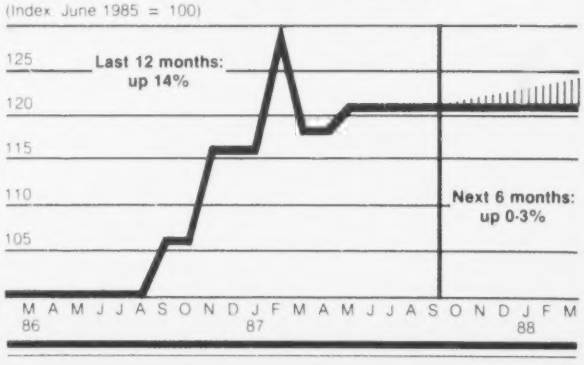
CURRENT SITUATION: Mills are posting new prices— Scheduled to move up are carbon sheet, carbon and high-strength low-alloy plate, stainless sheet and plate, and selected hot-rolled bar rounds. **Whether they stick depends on demand and continuing mill competition.** The proposed hike on ferritic alloy stainless sheet and strip has already been rescinded. Earlier supply tightness is easing.

DEMAND: The lackluster pattern is likely to continue. Second half domestic shipments will total only 32-33 million tons vs. the first half 36 million tons. **Only 68-69 million tons will clear the market in 1987** because of disappointing demand from construction and autos. But appliances remain strong and equipment is holding its own. **No dramatic change is likely in 1988.**

SUPPLY: Rising mill potential—reflecting full-scale USX output and resolution of production problems at other mills—suggests an easier supply and falling lead-times. The AISI capability utilization index shows that operating ranges will continue in the 70-80% range. One analyst estimates that the domestic industry would have to cut capacity by 15-20 million tons before any real long-lasting market balance could be achieved. Imports account for about 22% of apparent consumption.

PRICE OUTLOOK: Spotty weakness can't be ruled out by late fall or winter—despite recently posted increases. The supply situation is improving as demand may be edging lower. Some steel users may have overbooked recently—leading to possible cancellations. **The recent increases in flat-rolled products are not likely to hold.** In 1988, the industry will do well to match the anticipated 4% increase in overall industrial prices.

Cold rolled steel sheet (Market price)



R&D still ranks high

Research and development is still high on the list of management priorities.

This year, U.S. firms (as reported in a new DRI-McGraw-Hill survey) plan to shell out $87 billion—nearly 5% more than they spent in 1986. Even subtracting 3% for higher prices, there's still room for a real gain of 2%.

Chances are the trend will continue beyond the current year. Preliminary plans, which are normally underestimated because they aren't always finalized so far in advance, call for an additional 4% increase over the 1988-1989 span.

Although these are smaller gains than noted over the past decade, they are nevertheless significant. Combined with the weaker dollar, they should make our products more competitive in domestic and world markets.

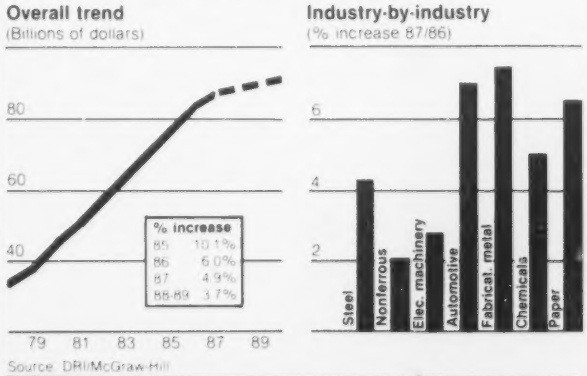
The encouraging R&D picture can also be appreciated by looking at the R&D/sales ratio. This year, the typical firm plans to spend 3.5% of its sales dollars on R&D. That's the same as last year and well above the 2.1% low hit in 1977 and 1979.

R&D also looks quite favorable when compared to capital investment. This year, a 22.3% R&D investment ratio is anticipated for all U.S. business—fractionally above last year and well above the 15% low in 1979.

But R&D averages tell only part of the story—there are substantial industry-by-industry variations. On a pure dollar volume basis, the aerospace and electrical machinery sectors lead the pack—matching each other and together accounting for 44% of total outlays.

On a percentage basis, aerospace (with a targeted 5.8% dollar increase for 1987) is far larger than the anticipated machinery gain. Other bigger-than-average 1987 dollar gains are projected for autos (7%), fabricated metals (7.5%), instruments (6.3%), paper (6.4%), rubber and plastics (11.2%), and petroleum (15.3%).

R&D spending: Two views



Computers

More competition seems to be shaping up in PCs as new models hit the market. IBM's new PS/2 Model 25—aimed at the education market—is listed at $1,350-1,695. But IBM has intimated that the more expensive model can be had for 40% off list. Tandy has introduced a powerful new Model 4000 (based on the 80386 microchip) which is priced at about 20% under similar machines from IBM and Compaq. The company has also introduced its first IBM-compatible laptop (the 1400LT) priced at $1,400, which will compete with models from IBM and Toshiba.

Electronic components

Don't expect any major runup—at least as far as overall price averages are concerned. Best bet: about a 3% increase over the next 12 months. Reasons: 1) OEM demand increases will be relatively moderate, 2) capacity utilization rates aren't that high, 3) material and labor cost pressures remain muted, and 4) international competitive forces still have to be reckoned with—as non-Japanese competitors on the Pacific Rim try to increase their market shares.

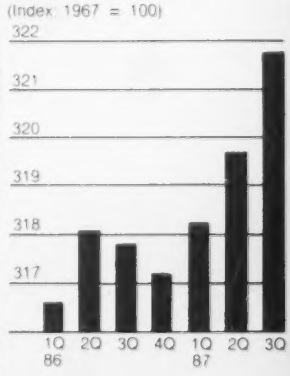
Methanol

Prices continue to firm. Reason: A combination of 1) good demand from formaldehyde and MTBE users and 2) snug supplies. If there were a plant problem, things could really turn tight. In any event, quotes which were in the 30-32¢/gallon range as recently as June, are now up as high as 34¢/gallon. And another increase can't be ruled out over the next month or so (into the mid-30s range)—as demand begins to show its normal seasonal pickup.

Building products

A mixed picture here—overall prices for materials and components for construction are expected to be only about 1% this year. Cement markets, in particular, continue to be weak both because of a leveling off in construction activity and import competition. At latest report, the material was fetching fractionally less than a year ago—with the average quote put only in the $64/ton range. Lumber has been holding up well—despite some falloff in housing starts. Thus spot tags for 2x4s are still close to 10% above a year ago. But some declines are likely here once the summer building season ends.

Building materials and components



PW PREDICTS

Paper

CURRENT SITUATION: Prices are edging higher. Witness 1) a $60/ton boost in coated groundwood to $720/ton, 2) a $40-60/ton increase in coated free sheet, 3) a $40/ton advance in newsprint to $570/ton, and 4) a $40/ton increase in uncoated xerographic papers. **Behind these advances: operating rates in the 90% + range and continuing strong demand.** Production in most paper and board sectors is running ahead of last year's levels—with unbleached linerboard leading the advance at 6%.

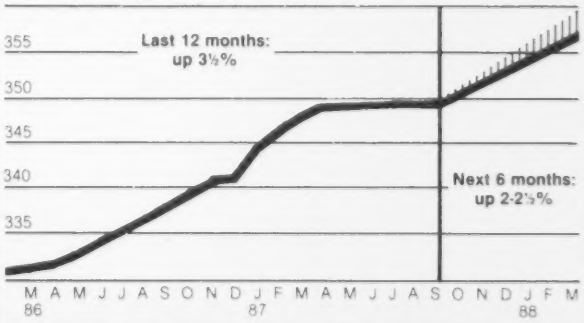
DEMAND: Gains should continue—pushing the overall 1987 paper and board production total to above 73 million tons—up 3% from 1986. Consumption (including net imports) will be 80 million tons, up 3%. Exports could be up 8%. Some production advances seen for 1987: Unbleached kraft linerboard (3%), solid bleached board (3%), recycled board (2.5%), newsprint (2%), uncoated groundwood (2%), uncoated free sheet (4%), coated papers (3.5%), and unbleached kraft paper (1%). **Preliminary signs for 1988 point to a bigger 3.5% overall output gain.**

SUPPLY: There should be enough—as the industry announces almost a million tons of new capacity for 1988-1989—over and above the 2.5 million ton increase indicated in last fall's American Paper Institute survey. But operating rates will remain high. Only coated papers are in more than ample supply—reflecting recent new capacity additions.

PRICE OUTLOOK: Most of the boosts above will hold. Chances are that mills will also push for a $30/ton linerboard hike—something which could put additional upward pressure on corrugated boxes. But then prices will begin to level off—with overall tags expected to be up by only 2-2.5% by early next year. The estimated increase for 1988 should not be more than 3.5%—except for corrugated which could advance by 5%.

Paper & product prices

(Index 1967 = 100)

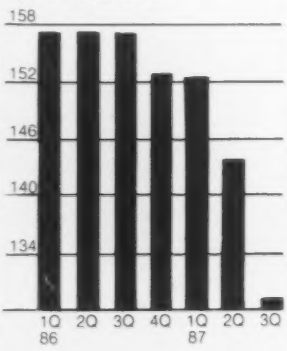


Sulphur

Prices have dropped for the second time this year—with a $7/ton reduction bringing prices down to around $127/ton FOB Tampa. This has occurred despite good demand—consumption so far this year has been running 8% above 1986 levels. Probable reason: The lower Canadian prices of recent months. But the trend could be reversed soon since Canadian quotes have begun to rise about $8/ton (to $100) in recent weeks. Also indicative of a possible upward shift: a strengthening fertilizer industry, especially in exporting where an increase of 600,000 tons of product is projected for 1987.

Sulphur

(FOB Tampa $/ton)



Aluminum

Prices continue to edge up. Ingot now commands about 75¢/lb. And recent boosts have been posted on extruded products and some auto sheet items. Producers have shifted to a price-at-time-of-shipment policy, too. Behind the firmness: snug supplies, with North American stocks down 11% over 1986. Demand has been firm, too—with U.S. shipments expected to rise 2% this year, to 15.75 billion pounds. But counterbalancing this are plans for higher North American output as mothballed potlines come back on stream.

Copiers

Look for fall introduction of digital full-color models that combine the technology of digital scanning, laser printers, and existing color office copiers. Cost of these machines, which are capable of high-fidelity color copying, is put at around 50¢/page, well under a slower photographic process that costs up to $1/page. The new machines will range in price from $10,000-35,000; demand should be brisk. By 1990, according to Dataquest, an electronic research firm, sales should be running around 20,000 machines per year.

Tantalum/ columbium

Prices are heading up. In the tantalum sector, higher ore quotes have made for about 4.5% average increases in sheet, wire, rod, bar, and tubing. And more advances are possible—with ore producers expecting a $25/lb tantalite quote before long—considerably above the current $19-22/lb range. Columbium and columbium/1% zirconium products are up by 6.5%.

Circle 361 on card

Machine tools

Cut-throat competition is still the order of the day—as low import quotes persist. One reason is the substantial volume of foreign inventories in the country when voluntary restrictions went into effect last year. These inventories are still in the process of being worked off. Official import prices are up, but they don't always reflect actual transaction levels. Some Japanese firms are reportedly still trimming nearly 35% off prices for large machining centers that list for $380,000.

Copper

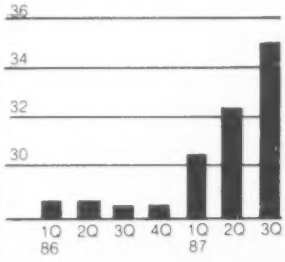
The first sustained rally in years has pushed the red metal up into the low 80s—the highest price in four years. Behind the advance are reduced inventories (stocks in Comex and IME warehouses are at their lowest levels in several years) and good demand from brass mills and wire and cable fabricators. Then, too, there have been some temporary shortages in spot metal and secondary material. Output is beginning to rise, so inventories should stabilize and perhaps begin to rise by yearend. Prices aren't likely to advance much further—and could well edge down before the year is out.

Textiles

The trend up the price ladder continues. Wool fabric quotes are spearheading the advance—as sharply higher raw wool prices make for increases ranging anywhere from 5-27%. Biggest boosts here are in the fine worsteds—the kind that go into suit fabrics. Cotton fabrics are also more expensive as higher import and raw cotton prices (now in the 70s) put upward pressure on the market. Some synthetic fibers such as rayon staple, selected nylon filaments, and spandex have also increased.

PVC pipegrade

(market price ¢/lb)



Polyvinyl chloride

Another 1-2¢/lb increase has pushed the pipe grade up into the 36¢/lb range—far above the 28¢/lb low of late 1986. Other grades are up, too—the general purpose suspension grade is at 37¢/lb and the film-wire-cable grade is at 38¢/lb. Behind the advance: rising chlorine costs and good demand, which is expected to be up at least 5% this year. Supplies remain adequate—as reduced bottlenecking in several plants brings nameplate capacity up to more than 8.7 billion lb this year (vs. 8.4 billion in 1986)—enough to prevent operating rates from rising above 90% for the year as a whole.

Plastics outlook

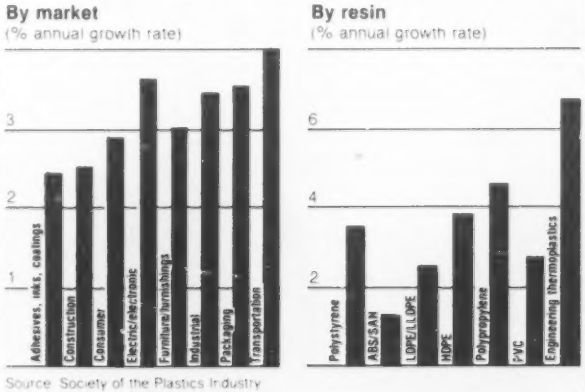
Figure on buying more plastic resins for production in the years ahead.

The 3.1% gains anticipated for the next 15 years won't be as spectacular as the 6.3% annual growth rate from 1970-1985. But it still adds up to a lot of material. By 2000, 75.6 billion lb of these versatile synthetics should clear the market—58% over the estimate for 1985.

The new projections, prepared by Chem Systems for the Society of the Plastics Industry, show virtually every industry sector and key resin sharing in the continuing gains (see chart). Some of the study's more important observations and conclusions:

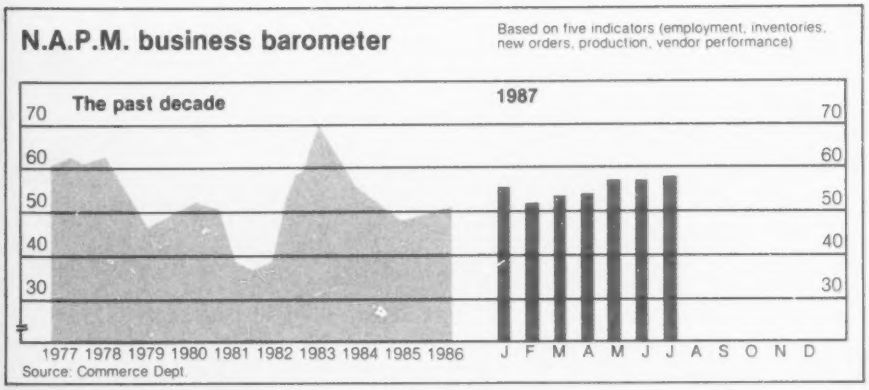
- Plastics will continue to make significant inroads in nondurable goods—e.g. packaging—at the expense of glass, paper, and metal.
- Resins should continue to replace traditional materials in consumer durables, making inroads in structural and semi-structural applications. Plastics will be increasingly used in initial designs—especially for automotive body panels and components (e.g. fascia, air dams, headlights, and spoilers).
- More emphasis on alloys, blends, additives, polymer modification in the reactor, and composites will enable firms to design polymers for individual applications, further stimulating substitution.
- Plastics fabrication machinery should reach $1.4 billion by 2000—an average annual growth rate of 5.1%.
- Thermoplastics with large-volume growth include polyethylene, polypropylene, PVC, and polystyrene. On a percentage basis, engineering plastics (projected to grow 6.6% annually) will lead the pack.
- The U.S. will be the principal geographic region for the next round of expansion in commodity plastics. But Asia will be a site for new engineering plastics plants.

Plastic demand trends through 2000



Source: Society of the Plastics Industry

BUSINESS DATATRAK


N.A.P.M. business barometer
Based on five indicators (employment, inventories, new orders, production, vendor performance)
The past decade
1987
70
60
50
40
30
1977 1978 1979 1980 1981 1982 1983 1984 1985 1986
J F M A M J J A S O N D
Source: Commerce Dept.

KEY ECONOMIC TRENDS

Slowly but surely upward

Next month will be a milestone—the 59th consecutive month of business expansion. This is an all-time high for peacetime.

There is nothing looming on the horizon to indicate any imminent change. Thus the N.A.P.M. Business Barometer, a time-tested indicator of activity one and two quarters ahead, continues to rise (see chart). Last month it moved above 58—more than 8 points above the neutral 50 mark and the highest in over three years.

Several factors contribute to this bullish reading. Plant and equipment spending seems to be bottoming out—partly because the initial negative impact of tax reform has subsided and partly because of higher profits. The latter, expected to be up more than 10% this year, should provide the wherewithal and psychological impetus for more capital spending.

New orders are also looking up. Bookings have been stable for six months, assuring additional gains in factory output over the upcoming fourth quarter.

Consumer demand leaves something to be desired—particularly in the auto sector where sales this year aren't likely to top 10.3 million units. That's more than 10% under last year's 11.6 million total.

Big ticket items such as appliances seem to be moving well. The same is true of other goods—as the typical family saves only 3.2% of its take-home pay (see chart). That's one of the lowest percentages in history.

Moreover, there's little to indicate that this rate will rise above 4% soon. Combine this with the current year's projected 5% rise in disposable income, and it virtually assures continuing gains in overall retail sales.

The international trade picture has also turned more favorable—at least as far as its contribution to GNP growth is concerned. Real net imports are now in a falling trend. This fact cannot be underestimated. More than 40% of the nation's real growth since last year is attributable to this trade shift.

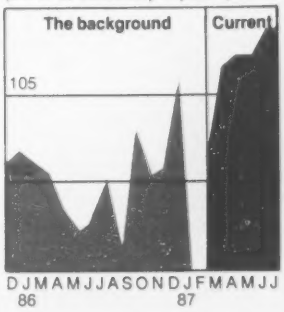
Inventories are also encouraging. As of latest report, they were surprisingly trim on the factory level—with the key stock/sales ratio in the 1.6 range, unchanged from year-earlier readings.

The implication is clear: Most of the new increase in orders alluded to earlier will be quickly translated into new production, thus further priming the pump.

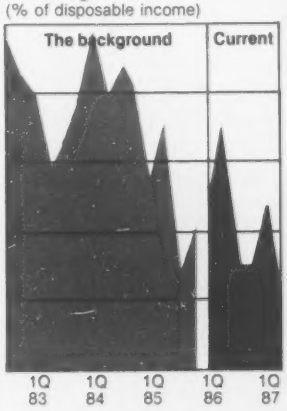
That's why *PurchasingWorld* projections call for a 3% rise in industrial production in the months immediately ahead. While hardly spectacular, this is considerably above the 2.3% rate noted over the first six months of this year.

Leading indicators

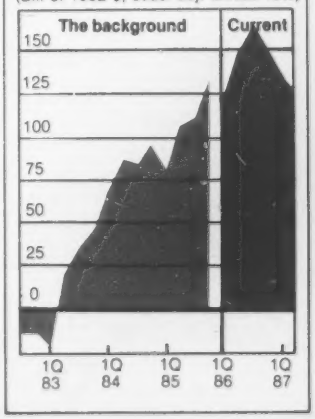
1. Durable goods orders
(Bil. of $, seasonally adjusted)



2. Savings ratio
(% of disposable income)



3. Real net imports
(Bil. of 1982 $, seas. adj. annual rate)



This is not to say that the economy will be problem-free. The huge budget deficit could easily edge higher again in fiscal 1988. And there's continuing uncertainty about oil. Consider also that the current business upswing is entering its sixth year—nothing goes on forever.

Nevertheless, there is little to indicate a major change in direction. Barring the unforeseen, the economy should continue its slow climb through 1987 and into 1988.

Electronics surges upward

Electronic equipment demand should increase 8% or more this year—far above last year's anemic 1% advance. And production gains may hit double digits in the commercial sector (computers, communication equipment, etc.).

This rosy forecast by Henderson Ventures carries over into 1988, too. Analysts at the Los Altos, CA, market research firm see a 12%+ overall gain for next year.

Within the fast-growing commercial sector, computer and office equipment-related items are likely to perform best. Watch for an 11.4% gain this year. New products by IBM and DEC are expected to act as a demand spur. But it will not be until 1988 that capital spending sufficiently recovers to provide an enthusiastic response—about 15% is estimated—to the new offerings.

Elsewhere in the commercial sector, communications apparatus won't fare badly either. This year's 8.4% advance will accelerate to over 13% in 1988. Ditto, industrial equipment and instruments where gains of 10.4% and 15.8% are seen for 1987 and 1988.

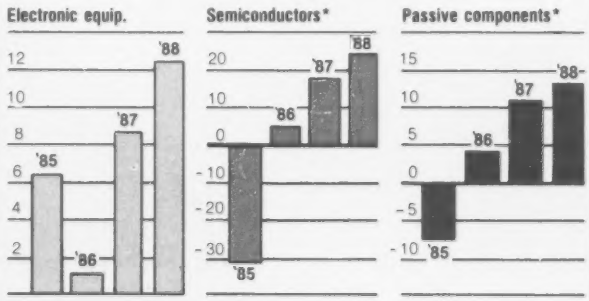
The outlook for non-commercial items is more mixed. While consumer items are expected to move well—up 9.3% and 15.8% in 1987 and 1988—military equipment over the same two-year period will show little more than a 4% average annual gain.

All this suggests double-digit growth for the electronic components that go into all these products. Henderson Ventures pegs merchant market semiconductor growth at around 19% this year—and at 24% for 1988.

The picture is similar for passive components, though the rates of growth are lower. Purchases this year are projected to rise 10.7%—to be followed by a 14% advance in 1988.

Electronics demand heads higher

(% increase in current $ terms)

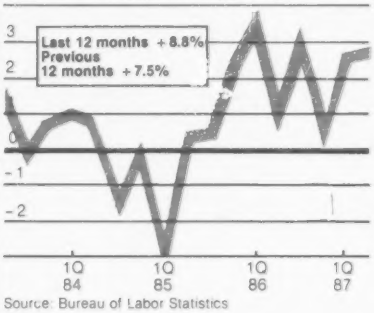


* Merchant market purchases

Source: Henderson Ventures

Import prices: the trend is still up

Overall (ex. fuel)
(% increase over previous quarters)



Product by product
(% increase over past year)

Textiles 5.6
Steel bars, rods, shapes 5.4
Fasteners 8.8
Tools 5.4
Elec. motors and gener. 11.3
Textile mchy. 20.8
Printing mchy. 20.9
Metalworking mchy. 17.1
Heating and cooling eqpt. 6.6
Pump & compressors 11.7
Mechanical hand. eqpt. 19.0
Bearings 6.2
Office mchy. 5.0
Elec. mchy. 8.3
Autos 8.6
Electronic compon. 3.9

Source: Bureau of Labor Statistics

Import prices reflect dollar's drop

Import prices continue to creep up—reflecting the lagged effects of the steady dollar devaluation since 1985.

Even if you remove the distorting impact of recent oil boosts, the increase over the latest 3-month period comes to 2.6%. And over the past year, the advance has been close to 9%.

Compare that to the much smaller rise in domestic producer prices over the same period, and it suggests that import bargains may be harder to find.

A more detailed import price rundown for the latest quarter (April to June) follows:

- **Chemicals:** The overall advance came to 3%—similar to the previous quarter. The year-to-date rise in this index contrasts with the steadily declining prices over the previous three years and is attributable to price rises in oil-based organic chemicals.
- **Intermediate products:** Quotes jumped 3.7%—and have increased 8.7% over the past year. Nonferrous metals, led by silver, were up 10.3% over the last three months. And iron and steel rose 3.9%, following a 3.2% 1Q gain. Large boosts were also posted for cork and wood (5.1%), non-metallic mineral manufactures (3.9%), and leather (4.7%).
- **Machinery:** Prices rose 1.8% compared to a 3.1% increase over the previous quarter. Road vehicles were up 1.6% vs. 2.9% in the first quarter. Also decelerating were general industrial machinery (2.1% vs. 5.8%), and electrical machinery (1.3% vs. 2.1%). But office machinery and telecommunications equipment showed somewhat larger 2Q increases.
- **Miscellaneous manufactures:** Increases over the past quarter were noted for plumbing, heating,

and lighting fixtures (4.1%), professional and scientific equipment (3.1%), photo apparatus, optical goods and watches (2.3%), and furniture (.5%).

The biggest increases were in the energy sector, which jumped 10.3% during the second quarter. This follows even larger 14.3% and 29.4% boosts for the previous two quarters. This area is now sporting import prices some 46% ahead of a year earlier.

CURRENT PRICES

Energy boosts prices

Industrial producer prices accelerated last month. Much of the impetus can be traced to energy—though this time some modest boosts were also posted in metals, textiles, petrochemical derivatives, and some paper products.

Most analysts, however, are not concerned. They think the energy increases could be about over. Ditto those posted on nonferrous metals. More important, despite these recent advances, overall industrial averages are up only 4.5% *vis a vis* year-earlier levels.

The year-to-year increases are heftier in the energy and nonferrous metals sectors, where current tags are up 14% and 12%, respectively. But keep in mind that both these areas were extremely depressed last year. In both cases, quotes are still well under highs of a few years back.

A more detailed rundown on specific changes over the latest 30-day period follows:

- **Energy:** Prices moved higher in almost all areas—including crude oil, gasoline, residual fuel, home heating oil, jet fuel, liquid petroleum gas, and electric power. The only exceptions were natural gas and coal, where small declines were noted.
- **Metals:** All major nonferrous metals—including lead, copper, aluminum, and zinc—were sharply higher. Ditto nonferrous mill shapes and most metal scrap. Steel, however, remained relatively unchanged, though some increases are scheduled over the next month or so.
- **Other durable materials:** On the up side were electronic components, nonferrous wire and cable, and lumber. But metal containers, hardware, and motor vehicle parts all edged lower.
- **Nondurable materials:** Industrial chemicals were

This month's breakdown

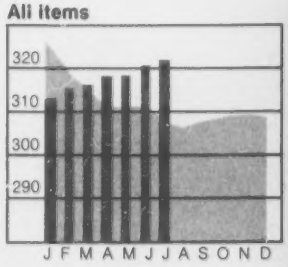
	Latest level (July)	% change from: Month ago	Year ago
Bearings	356.8	0.3	−0.1
Bolts, nuts, etc.	278.5	0.0	0.6
Chemicals, inorganic	294.7	1.1	0.2
Chemicals, organic	360.9	−1.4	11.7
Concrete products	326.0	0.1	0.1
Corrugated cartons	296.3	0.2	12.3
Cutting tools, small	293.1	0.0	0.3
Electric lamps (bulbs)	347.5	0.0	0.0
Electronic components	204.0	1.1	0.8
Fans and blowers	370.7	0.2	1.4
Foundry and forge products	363.7	0.0	0.0
Fuel oil (residual)	688.5	5.8	58.6
Furniture, commercial	326.6	−0.1	2.6
Gasoline	414.9	2.6	31.0
Glass, flat	237.6	0.2	1.7
Glass containers	402.1	0.3	0.2
Gypsum products	316.9	−3.5	−9.4
Hand tools	395.7	0.2	3.2
Hand tools, power driven	240.7	−0.4	1.2
Industrial furnaces	402.2	0.0	1.8
Integrating and measuring instruments	240.9	0.5	2.3
Internal combustion engines	359.2	0.1	1.5
Lubricating oil	345.1	−1.0	−7.6
Lumber millwork	331.4	0.5	3.3
Material handling equipment	294.4	0.2	0.8
Metal containers	357.7	−0.7	−1.3
Metal mill shapes (nonferrous)	321.1	3.3	7.1
Metal tanks	303.5	1.3	1.4
Motors and generators	357.0	0.4	1.2
Motor trucks	319.4	0.2	4.3
Office and store equipment	158.9	0.1	2.8
Paperboard	296.3	0.4	8.9
Paper boxes and shipping containers	287.2	0.2	7.3
Paper office supplies	242.3	0.0	1.8
Paint	283.8	−0.1	0.4
Plastic resins	324.2	4.0	9.3
Precision measuring tools	279.2	1.6	4.2
Pumps and compressors	366.9	0.3	1.4
Refractories	374.4	0.5	0.5
Rubber belts and belting	327.9	−2.2	−3.5
Scales and balances	234.3	0.1	1.3
Steel products	353.1	0.1	1.5
Switchgear	291.4	−0.4	2.2
Textiles, synthetic fibers	148.1	0.4	−1.2
Textiles, gray fabrics	158.0	2.0	4.4
Tires and tubes	232.2	0.5	−0.5
Transformers and power regulators	235.8	0.7	1.2
Welding equipment	305.6	0.6	1.1
Wire and cable	210.4	1.5	2.3

Industrial prices

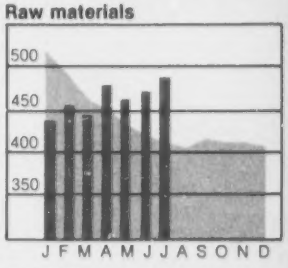
(Index: 1967 = 100)

1986 1987

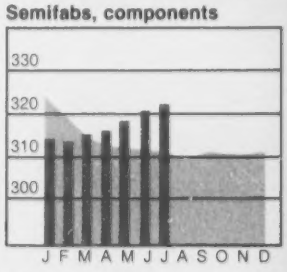
All items



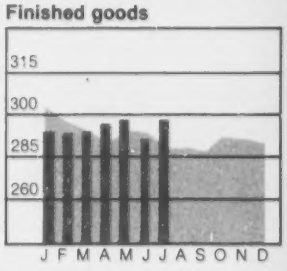
Raw materials



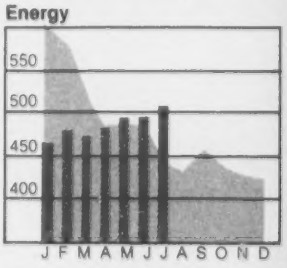
Semifabs, components



Finished goods



Energy



Source: Bureau of Labor Statistics

down—sparked by declines in benzene and styrene. So were inedible fats and oils, gypsum products, and rubber belts and belting. But offsetting these were increases in plastic resins, paint materials, synthetic fibers, gray goods, synthetic rubber, and much of the paper sector (including fine papers, paperboard, and paper boxes).

■ **Machinery:** Averages edged up only 0.1% over the month. But there were some notable increases in individual lines—namely precision measuring tools, transformers and power regulators, welding machinery, and integrating and measuring instruments.

STEEL SCENE

Bears brake demand

A modest leveling off in steel demand may be in the making by early fall.

That's not only being suggested by *Purchasing-World*'s own industry analysis, but by people at the grass roots level—industry buyers and distributors. As of now the latter, responding to a Steel Service Center Institute (SSCI) survey, are equally divided between those anticipating demand decreases and increases in incoming orders balance at 22%. The remaining 56% see little or no change.

Steel buying PMs are even more bearish. Replies to a similar question suggest that one out of four plans on a drop-off in his or her steel receipts over the next three months—far outweighing the 11% who feel some increases may be in order.

One reason for this is the flattening in construction and autos—two of steel's key markets. In the auto area, there's also a possibility of a strike. And many analysts predict that even if a strike is prevented, high auto inventories and an anticipated decline in car sales will force a retrenchment of auto production and therefore of steel consumption.

An inventory shift is still another possible braking influence on demand. An impressive 46% of steel buyers surveyed contemplate cutbacks in their steel holdings—nearly six times as many as the 8% who want to increase their stocks of the metal.

But it's doubtful whether this is realistic. Buyer inventories are currently equivalent to 1.82 months' supply—pretty close to the low of a month earlier and well under the near 2-month levels prevailing as recently as this past spring.

Another interesting survey finding: Service centers expect higher prices ahead. Right now, 9 out of 10 feel steel replace-

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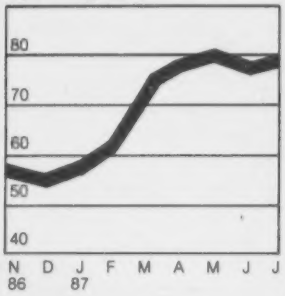
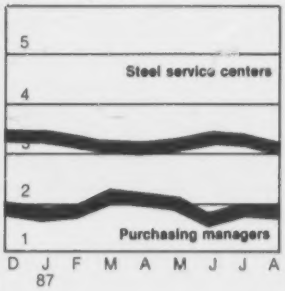
BUSINESS DATATRAK

Steel

Operating rates

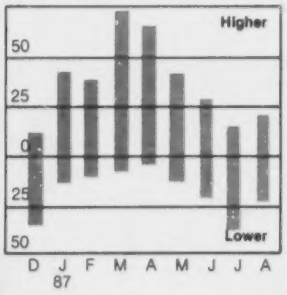


Inventories
(Months supply on hand)

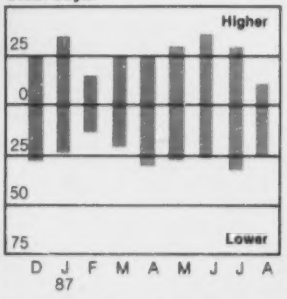


Demand
(Percent of respondents)

Service centers incoming orders



Steel buyer



Source: Steel Service Center Institute, NAPM Steel Buyers Committee

ment costs will be higher six months from now—12% put the advance in the 5%+ range.

One possible reason for this rising service center price forecast could be lessening competition from imports. Only 10% of surveyed distributors report imported carbon steel prices under comparable levels at this time. That compares to 34% in late 1986 and marks the lowest such percentage in years.

And the same diminishing import price advantage is seen for stainless, where only 26% now report lower-than-U.S. figures, compared to 75% last December and 90% a year ago.

Steel buyers, too, report less import price competition. Only 29% note price breaks now (vs. 37% late last year). And not one single respondent dubs the advantage as "substantial."

Nor is import price competition likely to heat up again. According to 7 out of 10 distributors, overseas mills are now actually less active in seeking new business. And buyers, responding to a similar question, agree.

But even with reduced import competition, the higher price tags projected by service centers for the next six months may not be attainable, because of the expected leveling off in demand alluded to earlier. This suggests that much of today's supply snugness (mainly in plate, hot-, cold-rolled, and coated sheet) is likely to disappear—thereby making it harder to post a significant price increase.

Factoring this demand variable into their equations, most econometric forecasting firms are now calling for only a few percentage points rise in steel prices over the next few quarters.

Import prices
(Compared to domestic)

Steel buyers

ABOVE	23%
SAME	48%
SLIGHTLY BELOW	29%
SUBSTANTIALLY BELOW	0%

Service centers (carbon)

ABOVE	6%
SAME	84%
5-10% BELOW	8%
10-20% BELOW	2%
OVER 20% BELOW	0%

PROCUREMENT STATUS

No problems in sight; supplies in control

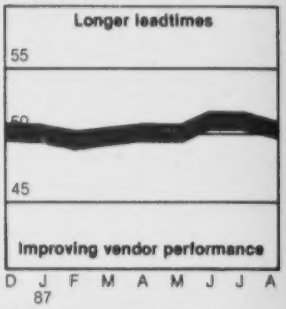
Leadtimes seem to be stabilizing after the slow rise of the last few months.

The N.A.P.M. Business Survey Committee reports that slower deliveries still outnumber faster ones. But the group goes on to add that much of this may be due to shortages in steel following the lengthy USX strike last year.

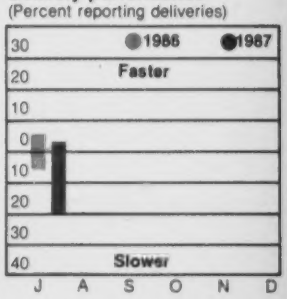
In any event, with these shortages expected to begin disappearing, it's hard to see any further deterioration in overall delivery performance. Also on a rosier note—*PurchasingWorld*'s leadtime index (a compilation of more than 150 product lines) has

Monthly procurement status report

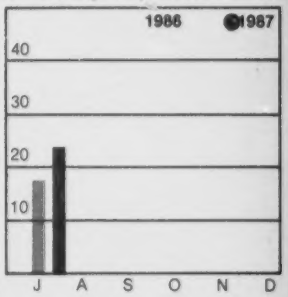
Leadtime index
A "diffusion" index based on 158 key commodities. Above "50" indicates a tendency for leadtimes to stretch out. Below "50" suggests improving vendor performance.



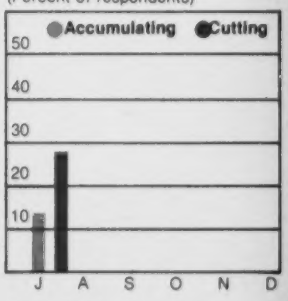
Delivery performance
(Percent reporting deliveries)



Forward commitments
(% committing 90 days or more in advance)



Inventory strategy
(Percent of respondents)



Source: NAPM

leveled off at the neutral 50 mark following four consecutive small monthly advances.

Still other indications that the procurement picture is now under control:

- Some 56% of queried buyers are now committing 30 days or less in advance for their production materials—about the same percentage noted in recent months.
- Inventory paring is again the order of the day, reversing the slight tendency toward accumulation noted last month. Obviously not too many PMs are concerned about stockouts.
- Only two items (aside from steel sheet and plate) are said to be in short supply—styrene and caustic soda.

Also indicative of adequate supplies ahead is the fact that the nation's industrial purchasing executives do not intend to cut back on imports—despite recent price hikes. For the remainder of the year, some 24% actually expect to step up their purchases and another 55% anticipate no appreciable change.

No big demand gains threaten to upset today's problem-free procurement environment. Preliminary indications suggest that fourth quarter production schedules will be increasing at only a 2-3% annual rate—hardly the type of gain to tax suppliers, many of whom are still saddled with excess production capacity.

Leadtimes and availability

Chicago: Minor shrinkages are noted. Included (in weeks) are offset paper (4-8), specialty text paper (6-8), sodium bichromate (½), and common process stearates (5). Previously extended steel leads are holding. Modest price hikes, too—in mill supplies and hardware.

Cleveland: Corrugated boxes have come in a week (to 2-3), and natural kraft is now available on demand. Ditto, most alloying materials, plastic shrink film, strapping, and steel drums. Other drums (2-ply fiber and steel canisters) can be had in 2 weeks. Ditto most lumber items, paint, and plastic resins.

Los Angeles: Moving out (to new weekly leads) are pumps (11-12), foreign fasteners (18-20), and custom seals and gaskets (5-6). Cardboard cartons have come in (to 3-5). No changes in galvanized steel (12-14), grey iron castings (6-8), brass castings (10-12), and aluminum tubing (4-6).

Houston: Several items are moving into the upper ranges of their leads—with possible stretchouts ahead. Included here are high-pressure heat exchangers, alloy and carbon steel exchangers, and shop fabricated steel pipe (both carbon and alloy). Extensions are also possible in component parts.

Philadelphia: Standard bronze valves have come in fractionally (to 5-6 weeks). Other weekly leads, basically unchanged, are: standard bearings (stock to 4), specialty bearings (12-14), standard fasteners (stock to 6), special fasteners (8-10), specialty FHP motors (10-12), and general usage electric meters (12).

Pittsburgh: These leads (in weeks) are typical: most alloying metals (2)—except for nickel (3) and zinc (4), mill quantities of copper products (4), polyethylene and PVC (5-6), paint (4-5), steel strapping (2-3), and lumber and corrugated boxes (3-4).

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BUSINESS DATATRAK

Leadtimes (in weeks)	Now	Month ago	Six months ago
STEEL			
Sheet (Phil)	4	4	4
C-R Sheet (Chgo)	11	11	10
Plate (Phil)	10	10	3½
Plate (Chgo)	13½	13½	4½
Reinforced (Hous)	6	6	6
H-R Bars (Phil)	5½	5½	5½
H-R Bars (Chgo)	11	11	4½
Cold-Drawn Bars (Phil)	5½	5½	5½
Galvanized (LA)	13	13	13
Galvanized (Chgo)	12	12	10
Structurals (Chgo)	5	5	4½
Structurals (Hous)	11	11	17
Tubing (Phil)	5½	5½	5½
Grey Iron Castings (LA)	7	7	9
Steel Castings (Hous)	11½	11½	11½
Forgings (Hous)	6	6	6
Pipe, Carbon (Hous)	17	17	17
ELECTRIC & ELECTRONIC			
Cables (Chgo)	8½	8½	8½
Capacitors (Chgo)	16	16	16
Circuit Breakers (Chgo)	6	6	6
Electromech. Devices (LA)	7	7	7
ICs (Linear) (Phil)	4½	4½	9
Motors (Phil)	9	9	9
Motors, 1000 hp & Up (Hous)	39	39	39
Printed Circuit Boards (Chgo)	9	9	9
Relays (Chgo)	15	15	15
Resistors (Chgo)	9	9	9
Resistors, Wirebound (Phil)	5	5	5
Transformers (Chgo)	10	10	10

	Now	Month ago	Six months ago
LUMBER			
Hardwood (Pgh)	3	3	3
Hardwood (Clev)	2½	2½	1½
Plywood (Chgo)	3	3	3
Plywood (Phil)	1½	1½	1½
Softwood (Clev)	2	2	2
Softwood (Phil)	⅛	⅛	⅛
Softwood (Pgh)	3	3	3
Particleboard (Phil)	2½	2½	2½
CHEMICALS-PLASTICS			
Adhesives (LA)	½	½	½
Naphthalene (Chgo)	2	2	2
Paint (LA)	4	4	4
Paint, Coil Coating (Pgh)	4	4	4
Paint, Maint. (Cleve)	2	2	2
Polyester Resin (LA)	2	2	2
Polyethylene Resin (Cleve)	2½	2½	2½
Polyethylene Resin (Pgh)	4	4	4
PVC Resin (Chgo)	2	2	2
PVC Resin (Pgh)	6	6	6
Titanium Dioxide (LA)	1	1	1
PACKAGING			
Bags, Kraft (Pgh)	5	5	5
Bags, Multiwall (Clev)	9	9	9
Bags, Multiwall (Pgh)	6	6	6
Cartons, Corrugated (Cleve)	2½	2½	2½
Cartons, Corrugated (Hous)	2	2	2
Cartons, Folding (Phil)	6½	6½	6½
Cartons, Folding (Pgh)	3½	3½	3½
Cellophane Wrap (Phil)	5	5	5
Plastic Bags (Pgh)	3½	3½	3½
Plastic Pkg. (Pgh)	3	3	3

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	Now	Month ago	Six months ago
Shrink Film (Chgo)	6	6	6
Shrink Film (Clev)	1	1	1
Drums, Fiber (Pgh)	1	1	1
Drums, Steel, Std. (Pgh)	1	1	1
Wood Pallets (Chgo)	2½	2½	2½
Wirebound Boxes (Pgh)	4½	4½	4½
Strapping (Clev)	1	1	1
Strapping (Pgh)	3	3	3
PAPER			
Fiberboard (Clev)	3½	3½	3½
Glassine (Clev)	4½	4½	4½
Glassine (Pgh)	5½	5½	5½
Groundwood (Clev)	4½	4½	4½
Groundwood (Pgh)	7	7	7
Kraft (Clev)	½	1	1
Kraft, Bleached (Clev)	1	1	1
Kraft, Bleached (Pgh)	5	5	5
Kraft, Natural MFNS (Clev)	½	½	½
Laminated (Clev)	8	8	8
Tissue (Pgh)	5½	5½	5½
NONFERROUS			
Aluminum Coil (Chgo)	19	19	13
Aluminum Plate (Chgo)	14	14	12
Aluminum Sheet (LA)	4½	4½	4½
Aluminum Sheet (Chgo)	19	19	13
Brass Castings (LA)	9	9	7
Brass Rods (Chgo)	7½	7½	9
Brass Sheet (Chgo)	11	11	5
Brass Tube (Chgo)	13	13	7
Copper Fittings (LA)	3½	3½	3½
Copper Mill Prod. (Pgh)	4	4	6

	Now	Month ago	Six months ago
Copper Tube (LA)	7	7	7
Copper Tube (Phil)	5½	5½	5½
Lead (Pgh)	2	2	2
Magnesium (Pgh)	2	2	2
Manganese (Clev)	1	1	1
Nickel (Clev)	1	1	1
Nickel (Pgh)	2	2	2
Silicon (Clev)	1	1	1
Tin (Pgh)	2	2	2
Wire, Specialty (LA)	5	5	5
Zinc (Pgh)	4	4	2
MISCELLANEOUS			
Bearings, Domestic (Phil)	2	2	2
Bearings, Foreign (Phil)	26	26	26
Boilers & Furnaces (Hous)	35	35	35
Compressors, Centrifugal (Hous)	50	50	48
Compressors, Reciproc. (Hous)	39	39	39
Fasteners (Chgo)	1½	1½	1½
Fasteners (LA)	8	8	7
Fasteners, Std. (Phil)	3	3	3
Heat Exchangers, Carbon-alloy Steel (Hous)	21	21	21
Heat Exchangers, Hi-pressure (Hous)	24	24	26
Insulation Mat'l. (LA)	7	7	7
Machined Parts (Hous)	9	9	9
Pipes & Valves (Chgo)	1½	1½	1½
Pumps (Hous)	21	21	24
Pumps (LA)	11½	11	11
Rubber, Synthetic (LA)	2	2	2
Rubber Hose (LA)	4	4	4
Tungsten Carbide Parts (Hous)	15	15	15
Valves, Cast Steel (Hous)	4	4	17
Welding Supplies (Hous)	5	5	5

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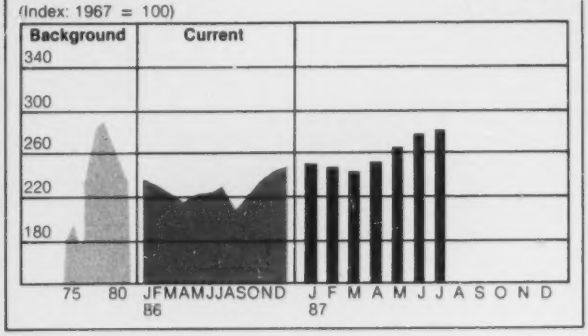
BUSINESS DATATRAK

Raw material price barometer

Latest month 283.5
Month before 276.4
Year ago 227.6

(Index: 1967 = 100)



Latest spot market prices

	Latest price	Previous month	Year ago
FERROUS METALS			
Pig iron, basic, valley, gross ton	213.00	213.00	213.00
Pig iron, Bessemer, Pitts., gross ton	213.00	213.00	213.00
Steel, billets, Pitts., net ton	367.00	367.00	367.00
Steel, structural shapes, Pitts., cwt.	23.90	23.90	23.90
Steel, structural shapes, Chi., cwt.	23.90	23.90	23.90
Steel, structural shapes, Los Angeles, cwt.	23.90	23.90	23.90
Steel, bars, dlvd. Phila., cwt., merchant quality	16.50	16.50	23.95
Steel, bars, Pitts., cwt.	16.50	16.50	23.95
Steel, bars, C.R., Pitts., cwt.	19.45	19.45	31.00
Steel, plates, Pitts., cwt.	19.75	19.75	18.25
Steel, plates, H.R., Pitts., cwt.	19.75	19.75	18.25
Steel, sheets, C.R., Detroit, cwt.	26.90	26.90	25.90
Steel, strip, C.R., Chi., cwt.	36.18	36.18	36.18
Steel, basic wire, Pitts., cwt.	23.65	23.65	23.65
NONFERROUS METALS			
Aluminum, ingot, lb. (market place)	.765	.725	.543
Antimony, N.Y., dealer, lb.	1.06	1.15	1.06
Beryllium-copper, cost ingot, lb.	5.65	5.65	5.65
Brass, red, 85%, [sheet], lb.	1.47	1.41	1.27
Brass, yellow, [sheet], lb.	1.42	1.36	1.22
Cadmium, N.Y., dealer, lb.	1.45	1.50	1.00
Copper, electrolytic, wire bars, refd., lb.	.83	.77	.63
Copper sheet, over 24 in., lb.	1.56	1.50	1.36
Lead, common, N.Y., lb.	.42	.40	.22
Magnesium, pig ingot, [99.8%], lb.	1.53	1.53	1.53
Mercury, 20 fl. lots, N.Y., fl.	300.00	295.00	190.00
Molybdenum, oxide, dealer, lb.	2.75	2.58	3.00
Nickel, cathode, dealer, lb.	2.32	2.18	1.82
Platinum, dealer, oz.	630.00	559.00	541.00
Silver, N.Y., oz.	7.76	7.65	5.39
Tin, N.Y., dealer, lb.	3.04	3.09	2.55
Zinc, Prime West, East St. Louis, lb.	.47	.46	.44
Zinc, die casting alloy, No. 3, lb.	.525	.525	.475
PAPER			
Uncoated book #3 offset, ton	860.00	860.00	850.00
Watermarked bond, ton	985.00	985.00	985.00
Gummed sealing tape, carton	16.98	17.01	16.34
Shipping sacks, ton	390.00	390.00	390.00
Solid bleached paperboard, ton	620.00	620.00	550.00
Kraft linerboard, 42 lb., unbleached, ton	350.00	350.00	310.00
TEXTILES			
Burlap, 10 oz., 40", N.Y., yd.	.240	.243	.229
Cotton drill, 1.85, 59", 68x49, N.Y., yd.	1.22	1.22	0.94
Cotton middling, 1", N.Y., lb.	.734	.719	.265
Printcloth, 48", 80x80, N.Y., spot, yd.	0.97	0.97	0.70
Army duck, 37", 13 oz., yd.	1.495	1.495	1.450
Blended printcloth, 64", 78x54, yd.	.94	.91	.74
20s combed yarns	1.98	1.97	1.70
Wool 64s, Staple, lb.	2.70	2.70	1.90
CHEMICALS			
Acrylonitrile, tanks, lb.	.395	.395	.395
Ammonia, anhydrous, tankcars, Gulf Coast, ton	105.00	105.00	80.00
Benzene, petroleum, tanks, Houston, gal.	0.95	1.35	0.68
Caustic soda, 76% solid, drums, carlots, cwt.	26.00	26.00	26.00
Cresylic acid [over 25%], tanks, lb.	.58	.58	.58
Formaldehyde, USP, 37%, [12% to 15% meth.], tanks, lb.	.106	.106	.106
Glycerine, synthetic, tanks, lb.	.81	.91	.91
Methanol, syn., tanks, 4,000 gals., f.o.b. Gulf Coast plants	.32	.30	.28
Naphthalene, crude, tanks, lb.	.22	.22	.22
Phthalic anhydride, tanks, lb.	.295	.295	.270
Polyethylene resin, low density liner film grade (market place), lb.	.345	.315	.255
Polypropylene, homopolymer grade (market price), lb.	.440	.400	.330
Polystyrene, general purpose grade (market price), lb.	.535	.530	.330
Polyvinyl chloride, pipe grade (market price), lb.	.340	.340	.300
Soda ash, 58%, light carlots, cwt.	6.15	6.15	6.15
Styrene monomer, 99.6%, tanks, lb.	.400	.425	.210
Sulphur, crude, ex-terminal, Tampa, Fla., lt.	127.50	134.50	157.50
Sulphuric acid, 66%, commercial, tanks, ton	66.86	66.86	66.86
Titanium dioxide, anatase, reg., carlots lb.	.77	.77	.73
Xylene tanks, gal.	.82	.90	.80
BUILDING MATERIALS			
Lumber, 2x4 fir, mbf, cl	331.50	329.30	317.70
Lumber 2x2 pine, mbf, cl	334.10	324.65	311.75
Plywood, plyform, ¾", msf, cl	585.15	580.75	592.05
Plywood, ⅜", msf, cl	389.00	384.15	385.50
Cement, bulk, ton, tl	64.25	64.35	64.43
Sand, ton, cl	7.17	7.21	6.62
Ready-mix concrete, 3,000 psi/cu. yd., 15 cu. yd.	49.08	49.08	48.01
Crushed stone, 1½", ton, cl	8.28	8.30	7.80
Concrete blocks, sand/gravel, 8"x8"x16", ea., tl	0.90	0.90	0.82
Gypsum sheathing, ½"x1"x8", msf, tl	228.23	228.77	217.57
Brick, common, per thousand, tl	198.26	192.26	185.51
Asphalt paving, AC-20	132.97	132.72	145.53
Concrete sewer pipe, 12", prem. joint, per foot, cl	7.51	7.48	7.23
FUELS			
Fuel oil, No. 6 or Bunker C, Gulf., bbl.	17.25	17.25	8.00
Fuel oil, No. 6 or Bunker C, N.Y., barge, bbl., reseller	21.75	20.25	13.50
Gasoline, 91 oct., reg., Los Angeles, rack, gal.	.600	.505	.405
Gasoline, 94 oct., reg., Chi., tank car, gal.	.605	.585	.460
Heating oil, No. 2, Chi., bulk, gal.	.567	.540	.445
Heating oil, No. 2, N.Y., bulk, gal.	.585	.553	.430
Heavy fuel, PS 400, Los Angeles, rack, bbl.	26.50	26.50	26.50
Jet kerosene, gal.	.540	.533	.400
LP-Gas, propane, Okla., tank cars, gal. [incl. discount]	.245	.245	.245
SCRAP MATERIALS			
Steel, No. 1, hvy., dlvd., Pitts., ton	89.00	83.00	76.00
Steel, No. 1 hvy., dlvd., Chi., ton	83.00	78.00	76.00
Copper, No. 1, East, wholesale buy, dlvd., lb.	.735	.705	.540
Copper, No. 2, East, wholesale buy, dlvd., lb.	.650	.620	.460
Brass, red, East, wholesale buy, dlvd., lb.	.695	.665	.500
Brass, yellow, East, wholesale buy, dlvd., lb.	.365	.345	.310
Alum., old sheet/cast, E., wholesale buy, dlvd., lb.	.490	.455	.325
Alum., mixed clip., E., wholesale buy, dlvd., lb.	.555	.510	.345
Zinc, old, East, wholesale buy, dlvd., lb.	.200	.200	.170
Lead, clean solids, East, wholesale buy, dlvd., lb.	.275	.275	.120
Paper, No. 1 mixed, dlr., N.Y., ton	Nom.	Nom.	Nom.
Paper, old corrug. box, dlr., Chi., ton	40.00	45.00	20.00
Paper, old corrug. box, dlr., N.Y., ton	25.00	25.00	18.00
Osnaburg cuttings, dlr., f.o.b. N.Y., lb.	.12	.12	.09
White wipers, No. 1, dlr. buy, f.o.b. N.Y., lb.	.23	.23	.11

[Sources: Metals Week, Engineering News-Record (20-city averages), Platt's Oilgram Price Service.]

for. If you don't sign Section 7, the carrier can come back to you for the freight charges, even if you shipped collect.

There are freight rate breaks at 500, 1,000, 2,000, and 5,000 pounds, and sometimes at 10,000, 20,000, 30,000, and 40,000 pounds for truck shipments and at higher weights for rail shipments. Whether shipping or receiving, keep in mind that if an order weighs 27,900 lb it may be cheaper to rate that shipment at the 30,000-lb rate. That means 2,100 more pounds would ride free. Purchasing or traffic managers should consider increasing such an order by about 2,100 lb if possible.

Companies should also develop a returned-material policy and provide customers with an authorization form. In that form, instruct your customers to include a copy of the packing slip with all returns so they can be immediately identified. Specify that UPS or truck should be used, depending on the size of the returned shipment. Don't allow air shipments without your permission. For shipments to be made by truck, give customers a list of your products and the corresponding descriptions to use on their bills of lading.

It is on inbound shipments that companies are most vulnerable to paying excessively for freight. Don't let every vendor ship small lots to you. You might look into the possibility of setting up one or several centrally-located consolidation points to which such shipments would be assigned. This operation will result in less congestion at your dock, less paperwork, and lower freight costs, without sacrificing service.

A seat belt manufacturer with plants in California, Texas, and Missouri purchased webbing from a vendor in Pennsylvania. From others it purchased steel stampings, steel hardware, and plastic parts. A consolidation site arrangement was set up in Chicago, since vendors were located in Illinois, Michigan, and Indiana. A contract trucker made a weekly run from the California plant, dropping off and picking up in Texas and Missouri, ending in Chicago where the accumulated freight was waiting. Of course, exceptions were made for parcel shipments and emergencies, which were shipped directly to the plants. Later, some of the vendors were replaced and a consolidation site was set up in Cincinnati—the new central location. The consolidator chosen at both locations was a local trucking company offering that service.

For more information about the Kandet Company's services **Circle 117**

Jack Flynn is president of Kandet Co., a traffic consulting firm in Waukegan, IL. He is also the author of Control Your Freight Costs.

Leased trucks may deliver tax benefits

Major industrial firms are taking another look at the lease-buy trucking decision. Reason: The recent changes in federal tax laws, namely, elimination of the investment credit, changes in depreciation, and the addition of a new alternative minimum tax (AMT) may tip the equation a bit further in favor of leasing.

That's not to say that taxes are the only factor in any final decision. Availability of cash, company service requirements, and a host of other factors also play major roles. But a new *PurchasingWorld* survey of lessors and lessees suggests that the ground rules have changed.

Taking off on this point, Ryder System's senior VP for corporate taxes, Harvey Smalheiser, feels the new IRS regulations have significantly reduced the tax benefits of ownership.

He goes on to say that every company must now pay a federal income tax—adding that under the AMT rules, deductions like accelerated depreciation are considered tax preference items which are added to a company's regular tax to arrive at alternative minimum taxable income. (Because trucks depreciate quickly, trucking operations are likely to fall into the minimum tax-paying position—and thus could cost more than paying the regular tax.)

The point to keep in mind is that the company must pay whichever is higher—the regular tax or the AMT. Ergo, for some outfits, leasing has become an increasingly attractive alternative.

Ryder is not alone in pointing out the pluses of leasing under the new tax law. John A. Simourian, president of the Lily Truck Leasing Corporation (a regional outfit headquartered in Boston) further ex-

plains: "The new rules place a 20% tax on half of the difference between the book income (income reported to owners) and taxable income (income reported to the IRS). This alternative minimum tax amount must be paid if it totals more than the new 34% corporate tax. This tax bite is startling when you purchase trucks and tractors using straight-line depreciation for tax purposes."

The difference between the new double-declining method of tax depreciation and the AMT 15% declining balance method creates excess tax depreciation and is subject to the minimum tax, Simourian adds.

"Leasing reduces the tax by closing the gap between book income and tax income," he concludes. "In both instances, leasing helps the customer avoid the additional tax burden."

More than just tax benefits

But all this talk about taxes should not overwhelm other leasing advantages, says the American Association of Equipment Lessors (AAEL). There are cash flow benefits, the hedge against obsolescence, flexible terms, and equipment expertise which maintain leasing's advantage, observes Michael J. Fleming, AAEL president.

"If we can't get our products out to our customers on time, we've got a major problem," says Tom Leonard, president of Yankee Foods, a New England-based food distributor which leases trucks to move products to its customers. "Our delivery system is one-third of our business—sales, delivery, and goods. We have to assure our customers that they will get the product in inventory and that we'll keep out-of-stock to a minimum. It's critical to have as little downtime as possible."

Had Yankee Foods decided to purchase its trucks, arrangements for service would have been required—either to contract out or to hire mechanics and provide the garage space required. "We find leasing simpler, more efficient, and more cost-effective," observes Leonard.

Harvey Smalheiser

Gordon J. Bingham

Companies like Yankee Foods that obtain full-service leases get more than trucks and service; they also get help in cost accounting, equipment and component specifications, insurance coverage, driver safety programs, licensing, and permitting.

At many regional and national truck leasing firms, there is a 24-hour driver hotline manned by trained professionals for drivers to call whenever a problem develops on the road. If service is required, it is immediately dispatched. Moreover, such computerized systems provide regular reports on equipment history and performance, allowing a fleet operator to check on the efficiency of both the truck and the driver.

Not for everyone

Nevertheless, truck leasing is not for every company. "Ownership for us is a good idea and it continues to be so," contends Sam Thurston, VP for distribution at Giant Foods Inc., Landover, MD. Giant is the dominant food retailer in the Washington, DC-Baltimore, MD metropolitan area.

"When we look at leasing, we look in terms of its being an alternate source of financing," says Thurston. "The numbers that we generate in a cost comparison have never been significant or substantial enough to make us change our position." However, he is quick to add that the new tax changes have not yet been considered in detail. Thurston contends that the main reasons for leasing do not apply to Giant.

On the other hand, there are a lot of firms which find truck leasing advantageous. Witness the fact that 15-20% of today's commercial fleet population (about 1.2 million vehicles) is currently leased. Zero in on the big trucks, and the figures are even more impressive, says Gordon Bingham, senior VP for strategic planning vehicle leasing and services at Ryder. He estimates that 25-30% of all new medium- and heavy-duty trucks fall under a leasing contract.

And the trend is up. Fleets leased by members of the Truck Renting and Leasing Association (about 75% of the industry) grew by 7.5% last year—on top of 1985's 9.4% advance. And there is considerable optimism about the future.

David Burr, president and CEO, Rollins Leasing Corp., Wilmington, DE, says many of his company's customers have expressed interest in long-term, full-service leasing since the new tax law was passed. These are customers who currently own, rather than lease, vehicles and with whom Rollins has contract maintenance agreements.

The AAEL, viewing truck leasing from a slightly different perspective, adds that 7.5% of total leasing business added last year was in new trucks and trailers—up from 1985's 6.9% level. Moreover, leasing as a

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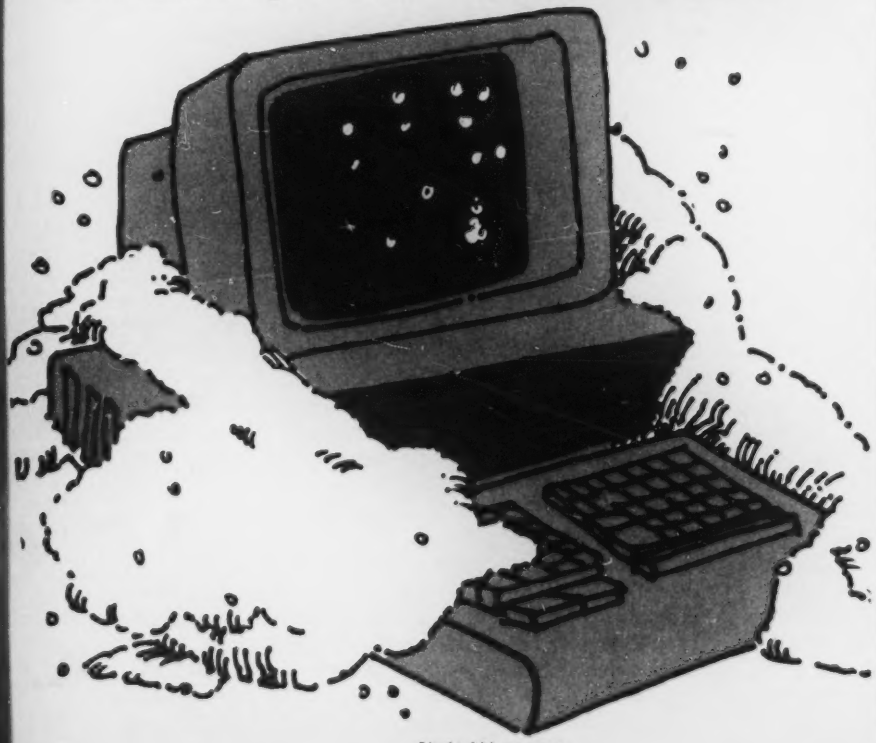


Circle 383 on card

TRANSPORTATION REPORT

whole, says the AAEL, is expected to grow $8 billion, or 8% from the 1986 total of $100 billion.

Leasing is nothing new

Many firms have been leasing trucks for quite some time. Data General in Westboro, MA, began leasing its road fleet requirements in 1981 when Robert Proulx (manager, corporate transportation, fleet operations) joined the firm.

"Our analysis disclosed that full service leasing was more cost effective in the long run compared to owning and contracting an outside maintenance operation," Proulx explains. "It reduced our staff requirements. When all factors are considered, we feel that we enjoy considerable savings."

The largest part of Data General's fleet operates nationwide, while the remaining units operate primarily in New England. The firm's over-the-road long-haul trailer rigs are leased from Ryder, while the remaining units are leased from Boston-based Lily.

"We felt that Data General would be best served by using a leasing firm with company-owned shops in our cross-country operations," Proulx adds. "On the other hand, Lily is in a stronger position to help us locally. Not only is leasing on the rise, but it's becoming more sophisticated." Ryder's Bingham says that the days when a leasing company could say, "Here are my standard leases and here are my rates," are pretty much over. Successful leasing companies are working to understand the customer's total transportation operation and then customizing a lease solution that best meets those needs.

Kenneth D. Simonson, chief economist and director of tax policy at the American Trucking Association Inc., Alexandria, VA, adds that leasing can sharply reduce a company's initial cash outlay and its requirements for support personnel like mechanics and drivers. Thus, he says, it is a viable option for many companies to consider.

Continued on page 69...

Wharton transportation report

Fall is a good time for hikes

Slowly increasing demand and fuel boosts that are somewhat higher than anticipated suggest some upgrading of previous 1987 freight rate hike forecasts.

Right now, Wharton Econometrics is pointing to a 3.6% overall boost, up from the 2.4% estimate made three months ago. But the increase is still quite moderate and is in line with inflation.

Much the same is expected for 1988, when a 3.7% advance is anticipated. Contributing to the continued modest rate of increase are relatively small hikes in labor costs, another year of modest increases in energy, continuing overcapacity in some sectors, and healthy intra- and intermodal competition.

A 5% rate of increase is expected for 1989 as costs rise and better supply-demand balance is achieved. But this advance is not excessive.

Here's a more detailed rundown of trends in individual transportation modes:

■ **Trucking:** It's a good demand year, with tonnage in one recent month running 10% above a year earlier. This suggests inroads into other modes.

On the cost side, diesel fuels are up about 5% from last year. But these rises will not be completely passed on. Witness the recent freight rate wars and continued industry discounting. Increases should average only about 3.5%. Next year, the pattern should be similar. But by 1989, mounting costs will bring a more robust 5.1% rise.

■ **Rail:** Traffic has increased only modestly, with carloadings up less than 2% this year. Shipments of grain, coke, and nonmetallic mining products have been way up, but motor vehicles and metallic ores have been off considerably.

Piggyback traffic is still advancing faster than overall freight, but the growth differential has narrowed. Rate increases should continue to show some acceleration, with 3.9% and 4.0% increases seen for this year and 1988.

Shippers using piggyback rail and truck combinations should benefit from a recent ICC decision to eliminate government rate controls over the truck portion of most intermodal shipments. This should help expand traffic and hold rate boosts.

■ **Air cargo:** Traffic has been running a healthy 6-7% ahead of last year. Rate increases are likely to be quite steep this year—advancing 4.6%.

Much of this can be attributed to both the big jump in traffic and a slowing down in the cut-throat passenger fare wars that almost always tend to spill over into the air cargo sector. Next year this spurt in rates will slow down to 3.6%.

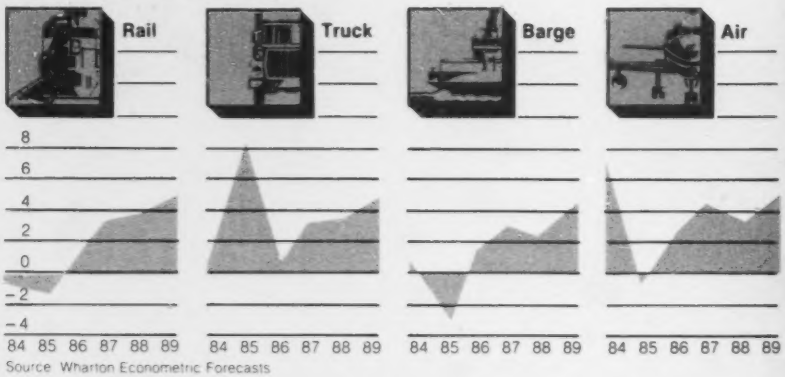
■ **Water freight:** The industry appears to have levelled off after five years of decline that claimed a large number of operators as victims. The survivors are much stronger than any of the competitors were before the decline.

However, the industry's rates will continue to be held down by the huge, albeit shrinking, surplus of barges that could still take years to work off through scrappage. Thus water freight rates—though advancing faster than last year's 1.6% pace—will continue to show the smallest gains of all modes.

This year, rates are expected to increase 3.1%, with similar advances next year. And even in 1989, when general economic pressure will be heating up, barge rates are forecast to increase only 4.3%. ***PW***

Freight cost outlook by mode

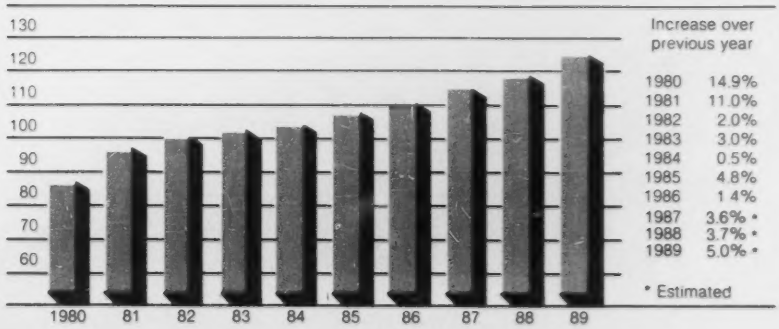
(Percent increase over previous year)



Source: Wharton Econometric Forecasts

PurchasingWorld freight rate index

(1982 = 100)



Increase over previous year	
1980	14.9%
1981	11.0%
1982	2.0%
1983	3.0%
1984	0.5%
1985	4.8%
1986	1.4%
1987	3.6% *
1988	3.7% *
1989	5.0% *

* Estimated

Survey of the month

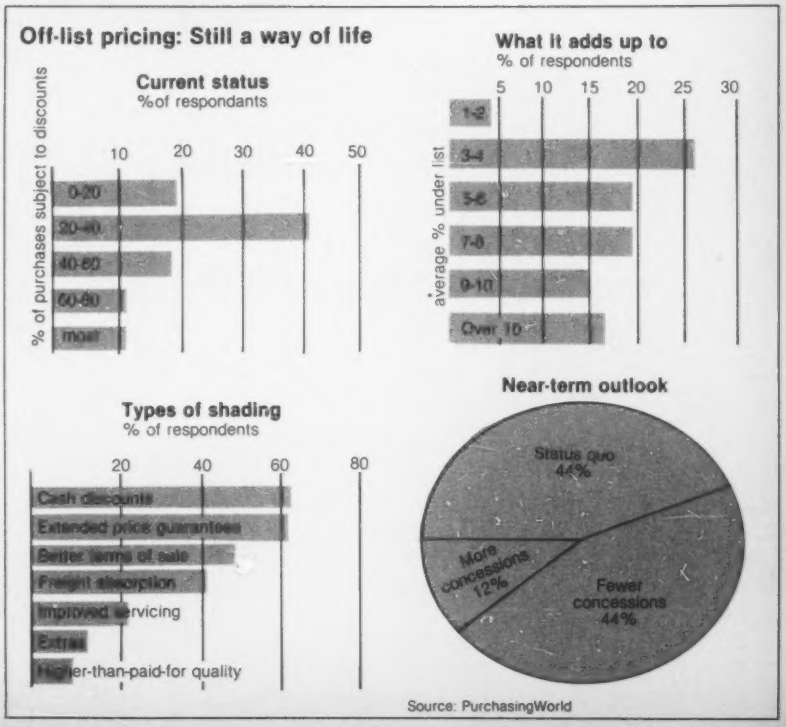
Bargain prices still abound

Although industrial tags are edging up, there are still plenty of off-list bargains around. If there are any doubts, *PurchasingWorld's* latest nationwide price survey should quickly lay them to rest. Not only are many quotes still negotiable, but the savings involved can be impressive.

Summing up the situation, Thomas Snyder, purchasing manager of Mansfield Plumbing Products in Perrysville, OH, says, "The truth is that many list prices do not reflect the true market value on either the wholesale or retail level. List prices today have very little credibility. Our procedure for major purchases has always been by competitive bidding—even when list prices were stable, had clout, and were supposedly unchangeable."

What this purchasing executive says is backed by survey results.

■ **Prevalence of concessions:** More than four out of five PMs say that at least 20% of their purchases are at



IN THEORY.

less than official list levels. And more than one out of five estimate that at least 60% of their buys are being shaded (see chart).

■ **Recent trends:** As might be expected, concessions are a bit harder to come by vs. last year, according to 37% of the respondents. But this is hardly an across-the-board development. Almost all the remaining respondents state that there has been very little change from 1986.

■ **Areas of price weakness:** Virtually every major sector seems to be involved—including steel, aluminum, copper and brass mill products, plastic resins, assorted chemicals, paper and products, motors, pipes/valves/fittings, computers, instruments, hardware, and transportation services.

■ **Reasons for concessions:** 59% of queried PMs attribute continuing deals to their own hard-nosed bargaining approach. Also prominently mentioned by about 45% of respondents are foreign competition, supplier gluts, and lackluster demand growth.

■ **Type of concesssion:** Two popular approaches are cash discounts and extended price guarantees, both noted by more than 60% of the survey respondents. Almost as prevalent were better terms of sale (48%) and freight absorption (41%). Also mentioned were improved servicing (22%), "extras" (11%), and higher-than-paid-for quality (7%).

■ **The overall impact:** Thanks to the above concessions, the average purchasing manager says he is paying 6% under list for his purchasing mix. More than three out of ten, for example, manage to shave at least 9% off book prices.

■ **A look ahead to 1988:** Most PMs feel that the recent trend toward reduced concessions will continue. Thus these survey projections: fewer concessions (44%), status quo (44%), and more concessions (12%).

Products singled out for fewer deals include paper and products, plastic resins, steel products, chemicals, and nonferrous metals. Some see more concessions in such hotly competitive areas as computers and other types of office machinery.

Whatever the product area, buyers seem determined to continue pressing for deals. Some feel order consolidation—with fewer suppliers—is the best route to this goal. Others plan either to continue playing one vendor against another or to explore the possibility of imports.

For the most part, the majority of PMs are still optimistic on the concession score—noting that while they won't have everything their way, they should have enough bargaining clout to assure continued off-list pricing.

Given today's ample capacity and slow demand growth, there's little to suggest anything but a continuation of the buyers' market of the past few years. Some of the items in current snug supply—steel, nonferrous metals, and some electronic components—could actually become easier in 1988. **PW**

IN PRACTICE.

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TRANSPORTATION REPORT

Source: American Association of Equipment Lessors, 1986 Membership survey, Ryder System, industry estimates

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Getting down to the nitty-gritty

The decision gets down to the fundamentals of how trucks are used, how much control is required over those trucks, and what service standards are needed, he contends.

Simonson observes, "If you own, you get the depreciation yourself. You get the residual value after the truck is paid for. But either way, you should be able to spec that truck according to what you want.

"Any shipper who has very detailed needs or a large volume is going to look at owning a fleet. That's the ultimate in control. It's also the ultimate in headaches," Simonson says.

So far nothing has been said about for-hire carriers—still another trucking option. Clearly, such carriers can deliver a load less expensively than privately operated fleets that are running half-empty with no backhaul.

But with those lower prices, Simonson notes, comes a loss of control over the shipment and slower delivery schedules: "If you're shipping in less-than-truckload amounts, your cargo will be taken to a consolidation terminal, to a breakbulk terminal, to a local terminal for delivery. It takes longer. So there is a price vs. service trade-off."

Finally, there's still another approach to trucking—the so-called trip-lease—leasing a driver and truck for specific trips. Independent operators as well as leasing companies often provide this service.

To sum up, then, there are many alternate approaches to trucking. But for an increasing number of shippers, (though certainly not all), the lease approach is gaining popularity because of tax and other considerations.

Some companies, for example, lease because they simply do not want the headaches of operating what amounts to a trucking business in addition to their primary business. Says Bob Schwartz, VP for sales and merchandising, King Super Markets, West Caldwell, NJ, "We're in the grocery business, not the transportation or maintenance business. We leave that to the experts." ***PW***

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